Real Estate Ownership and Investment in Saudi Arabia

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March 2017

The Saudi Vision 2030 (‘Vision 2030’) (and the related National Transformation Plan) sets out the Saudi Government’s plan to diversify the Saudi Arabia economy and address the challenges brought by low global energy prices.

Initiatives flowing from the Saudi Vision 2030 and National Transformation Program have been viewed as providing a powerful impetus to both the encouragement of foreign investment generally in the kingdom and also to the Saudi Arabia real estate sector, despite the declining oil prices and consequent cuts in government spending.

Against this background of apparent opportunity, this article outlines the rules on foreign ownership of real estate in Saudi Arabia and recent developments to encourage investment in real estate.

Saudi Vision 2030 and the National Transformation Plan

Vision 2030 maps out significant commitments by the Saudi Government relating to housing and the development of land for a variety of uses. In particular, Vision 2030 states: ‘Where it exists in strategic locations, we will also capitalise on the government’s reserves of real estate. We will allocate prime areas within cities for educational institutions, retail, and entertainment centres, large areas along our coasts will be dedicated to tourist projects and appropriate lands will be allocated for industrial projects.’

Under the National Transformation Plan (the ‘Plan’), the housing sector, with a budget of SAR 59 billion, is the biggest area of government expenditure. The Plan also has targets of:-

- increasing real estate sector contribution from GDP five per cent to 10 per cent;
- establishing partnerships with private sector developers to develop government land for housing projects; and
- establishing fast-track licences and special finance packages to encourage private sector investment in housing projects.

Ownership of land in Saudi Arabia

Ownership of land in Saudi Arabia is generally restricted to Saudis, but this is subject to certain qualifications. For example, Gulf Cooperation Council (‘GCC’) nationals and GCC companies have certain rights to own land, subject to a number of restrictions.

A GCC company (with shareholders who are all GCC nationals) or a GCC national may lease or purchase land to use it to conduct any licensed business activity from the land, and may own residential properties in Saudi Arabia, subject to a number of restrictions and conditions. However, these concessions do not apply to properties within the vicinity of Mecca and Medina.

As a matter of structuring, it should be noted that even the smallest equity interest held by a non-GCC entity will make a corporate entity ‘foreign’, triggering the requirement for a foreign investment licence, which includes conditions stipulating the amount of capital that must be invested and the timeframe for the investment by the foreign entity.

Additionally, foreigners (being non-GCC nationals or companies who are not 100 percent owned by GCC nationals) have certain rights to own land and property in Saudi Arabia. However, ownership is subject to a number of restrictions. One of the main issues is that foreign ownership of Saudi Arabia property must be linked to a particular project and is not a general right.

Structure for Investment in Real Estate

The Foreign Ownership of Real Estate Regulation (enacted by Royal Decree No. M/15 dated 17/04/1421H, corresponding to 19 July 2000G) regulates the acquisition by foreign, non-GCC nationals, of real estate in Saudi Arabia.

Under this regulation, the ownership and investment in real estate by a foreign investor is permitted, subject to obtaining a foreign investment licence from the Saudi Arabian General Investment Authority ('SAGIA').

A foreign company wishing to invest in real estate in Saudi Arabia will, generally speaking, need to establish a local Saudi Arabia registered entity (which can be wholly-owned by the foreign shareholders) in order to acquire title (either freehold or leasehold) to real estate in Saudi Arabia.

A foreign individual may own property in Saudi Arabia if he has normal legal residency status and has a permit from the Ministry of the Interior.

A non-GCC entity, generally, may own Saudi Arabia real estate that is reasonably required for:

- the conduct of its professional, technical, or economic activities, including for its headquarters or warehouses;
- private residences for housing employees of a licensed project; or
- residential use by individuals with normal legal residency status.

In addition, where the SAGIA licence permits, a non-GCC entity may own real estate in connection with a particular project for property development provided that, if the purchase of buildings or land is for the construction (by a Saudi Arabia licensed contractor) of buildings for investment purposes, whether through sale or lease, the following conditions must be complied with:

- the total cost of the project, both land and construction, may not be less than SAR 30 million (equivalent of USD 8 million); and
- the investment in the development must occur within five years of the purchase of the real estate.

In addition to the SAGIA licence, SAGIA approval must be obtained before the purchase of any specific property.

Foreign owned entities are restricted from acquiring any right of property in real estate within the borders of the cities of Mecca and Medina. There are also ownership restrictions where other regulations, resolutions of the Saudi Council of Ministers, and royal decisions expressly prohibit the acquisition of real estate in specified locations.

However, currently, if a foreign investor wishes to acquire completed, developed retail, commercial, or mixed use property in Saudi Arabia, for the purpose of holding as a real estate investment (rather than for the purpose of developing the property), then:

- there is no law that permits such acquisition by a foreign entity (even with SAGIA approval); and
- we are not aware of any instance where a foreign company has been permitted to acquire property in Saudi Arabia merely for investment purposes, without further developing the property

(in which case a real estate development licence, in addition to the minimum capital requirement and minimum timeframes to complete the development, are required).

Saudi Arabia also has a strict anti-fronting law, which must be carefully considered when structuring investments.

Recent Developments

In 2016, the Capital Market Authority introduced new rules allowing the formation of Real Estate Investment Traded Funds ('REITs') on the Saudi Stock Exchange (the Tadawul), in an effort to open the real estate market to investment by a wider range of investors. The rules cover the management, operation, and ownership of the REITs.

A REIT is a real estate investment fund:

- that is offered to the public;
- the units of which are traded on the Saudi Stock Exchange;
- where the primary investment objective is to invest in real estate developed through construction that generate periodic income, including residential, commercial, industrial, agricultural, and other types of real estates;
- which must distribute a prescribed percentage of its net profit in cash to the unit holders at least annually; and
- where the fund manager must appoint one or more appropriately licensed property management companies to manage the property held for investment.

The REIT property management companies should possess the necessary experience in real estate management, and should carry out the property management activities, including property management, property maintenance, leasing services, and rent collection. The fund manager may agree with a lessee in the lease contract that the lessee will manage and maintain the property during the leasing contract period.

Subscription in a REIT is open not only to Saudis but also GCC citizens and non- Saudi residents in Saudi Arabia. Non-resident foreign investors are also allowed to trade in the units of the REITs on the Tadawul.

The introduction of REITs has been regarded as part of the implementation of Saudi Vision 2030 and the National Transformation Plan. The new rules have the target of increasing real estate contribution from GDP five to 10 per cent annually and to provide private capital for the construction of around 1.5 million homes, as announced by the Saudi Government in June 2016 and planned over the next seven or so years.

Although the Saudi Arabia legal framework is quite restrictive on foreign ownership in real estate, it is hoped that the strong impetus given by Saudi Vision 2030 and the National Transformation Plan will see the introduction of greater flexibility in the rules. The introduction of REITs is a welcome step in the right direction.